

# Commonwealth of Puerto Rico

Comprehensive Annual Financial Report  
Year Ended June 30, 2012

## ***COMPREHENSIVE ANNUAL FINANCIAL REPORT***

*Fiscal Year Ended June 30, 2012*



*Commonwealth of Puerto Rico*

*Honorable Alejandro García Padilla  
Governor*

*Prepared by:*

*Puerto Rico Department of the Treasury*

*Melba Acosta Febo, CPA, Esq.  
Secretary of the Treasury*

*Karolee García Figueroa, CPA, Esq.  
Under Secretary of the Treasury*

This document is available on the Puerto Rico Department of the Treasury homepage  
On the World Wide Web: <http://www.hacienda.gobierno.pr>



**Commonwealth of Puerto Rico  
DEPARTMENT OF THE TREASURY  
San Juan, Puerto Rico**

Melba I. Acosta Febo, Esq.  
Secretary of the Treasury

September 16, 2013

To the People of the Commonwealth of Puerto Rico,  
Gov. Alejandro García Padilla and  
Members of the Legislature:

The Comprehensive Annual Financial Report (CAFR) of the Commonwealth of Puerto Rico (the "Commonwealth") for the fiscal year ended June 30, 2012 is submitted herewith in accordance with our responsibilities of reporting the Commonwealth's financial activities. To the best of my knowledge, the information presented provides a reasonable understanding of the state's financial activities. This report reflects my commitment to you, the citizens of the Commonwealth, to our Governor, to our elected officials and to the financial community to maintain and disclose our financial statements in a manner which fully conforms with accounting principles generally accepted in the United States of America (USGAAP) as established by the Governmental Accounting Standards Board (GASB).

The report is comprised of three main sections. The Introductory Section includes this letter of transmittal, general information about the Commonwealth, a list of the Commonwealth's principal elected and appointed officials, as well as an organizational chart. The Financial Section consists of the independent auditors' report, management's discussion and analysis (MD&A), the audited basic financial statements as listed in the table of contents with the notes thereto and the required supplementary information. The Statistical Section set forth contains selected unaudited financial and demographic information for the Commonwealth on a multiyear basis.

**PROFILE OF THE COMMONWEALTH**

As the governmental entity responsible for the preparation of this report, the Puerto Rico Department of the Treasury relies on information provided by the Commonwealth's financial and accounting management, in charge of ensuring that assets are safeguarded and financial transactions are properly recorded and adequately documented. The responsibility for both the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures, rests with the Commonwealth's management. To the best of our knowledge and belief, the information presented is accurate in all material respects and is presented in conformity with US GAAP. The presentation is designed to set forth the financial position and the results of operations of the governmental activities, the business-type activities, the aggregate discretely presented component units, the major funds, as well as the aggregate remaining funds of the Commonwealth as of June 30, 2012 with the respective changes in financial position and cash flows thereof, where applicable, and the respective budgetary comparison for the General Fund for the year then ended. We have included all the necessary disclosures to enable the reader to gain a thorough understanding of the Commonwealth's activities.

Agency funds consist of the Special Deposits Fund. This agency fund includes deposits under the custody of the Courts of Justice, Minors Support Administration for child support payments, deposits under the custody of the Commissioner of Insurance of the Commonwealth for escheated property, for insurance companies under liquidation and an allocated share of the sales and use tax corresponding to the municipalities.

### **CASH MANAGEMENT POLICIES AND PRACTICES**

The Commonwealth maintains a cash pool for its cash and cash equivalents. The balance in the pooled cash accounts is available to meet current operating requirements and any excess is invested in various interest-bearing accounts in the Government Development Bank for Puerto Rico, a discretely presented component unit. In addition, the Puerto Rico Government Investment Trust Fund (PRGITF) was created by the Commonwealth pursuant to Act No. 176 of August 11, 1995, as a no-load diversified collective investment trust for the purpose of providing eligible governmental investors of Puerto Rico with a convenient and economical way to invest in a professionally managed money market portfolio. The deposits on hand and the investments purchased are not collateralized, secured, or guaranteed by the Commonwealth or any of its agencies, instrumentalities, or political subdivisions.

The Commonwealth's investment policy is to minimize credit and market risk while maintaining a competitive yield on its portfolio. The cash temporarily idle during this year was invested mainly in U.S. government securities, stocks, corporate bonds, repurchase agreements, Commonwealth securities, other trading securities and short-term investments. These are primary government investments that are restricted and unrestricted.

### **CAPITAL ASSETS**

These basic financial statements include the capital assets of the Commonwealth. A discussion of capital assets accounting is included in the MD&A as part of the basic financial statements. More detailed information about capital assets can be found in the notes to the basic financial statements.

### **DEBT ADMINISTRATION**

The Commonwealth's general obligation and appropriation debt is currently rated "Baa3" with a negative outlook by Moody's, "BBB-" with a negative outlook by Fitch, and "BBB-" with a negative outlook by S&P.

Section 2 of Article VI of the Constitution of the Commonwealth provides that direct obligations of the Commonwealth evidenced by bonds or notes which are backed by the full faith, credit and taxing power of the Commonwealth shall not be issued if the amount of the principal and interest on such bonds and notes and on all such bonds and notes issued thereafter, which are payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year of such proposed issuance on account of bonds or notes guaranteed by the Commonwealth, exceed 15% of the average annual revenues raised under the provisions of the Commonwealth Legislation and deposited into the Treasury of Puerto Rico in the two fiscal years preceding the fiscal year of such proposed issuance. Section 2 of Article VI of the Constitution does not limit the amount of debt that the Commonwealth may guarantee so long as the 15% limitation is not exceeded through payments by the Commonwealth on such guaranteed debt. As of June 30, 2012, the Commonwealth is in compliance with the debt limitation requirement. Please refer to the computation of the legal debt margin in the statistical section of this report. More detailed information about the long-term debt can be found in the notes to the basic financial statements.

upfront payment of \$615 million. On July 24, 2012, the parties executed the lease agreement for the Airport and, on February 27, 2013, the parties successfully completed the financial closing. As a result of this transaction, on February 27, 2013, the Ports Authority received a lump-sum payment of \$615 million and will receive an estimated \$552 million in revenue sharing over the life of the lease. It is estimated that Aerostar will invest \$1.4 billion in the Airport during the life of the lease, including a commitment to invest approximately \$267 million in immediate improvements and comply with world-class operating standards.

The PPP Authority is currently evaluating projects for the development and construction of new infrastructure facilities. These projects include a rail transportation system from Caguas to San Juan and the extension of the PR-22 Highway from Hatillo to Aguadilla, among others.

#### **FINANCIAL CONDITION**

The MD&A, which can be found immediately following the independent auditors' report, provides an overview of the financial activities addressing both governmental and business type activities reported in the government wide financial statements. In addition, the MD&A focuses on the Commonwealth's major funds. Component units and fiduciary activities are excluded from the MD&A.

#### **OTHER INFORMATION**

##### **Acknowledgements**

The preparation of this report required the collective efforts, cooperation and support of numerous accounting and finance officials throughout the Commonwealth. Their dedicated efforts are sincerely appreciated.

The report could not have been accomplished without the professionalism and dedication of Jayson O. Padilla Morales, as well as the rest of the personnel of the Central Government Accounting Area, and Jorge Clivillés and Denisse Rodríguez from GDB, among other officials. This report reflects their collective efforts and is issued in compliance with the highest standards of financial accountability.

Respectfully submitted,



Melba Acosta Febo, CPA, Esq.  
Secretary of the Treasury

## COMMONWEALTH OF PUERTO RICO

### PRINCIPAL OFFICIALS

**Alejandro García Padilla**  
Governor

#### Members of the Cabinet

**Ingrid M. Vila Biaggi**  
Chief of Staff

**David E. Bernier Rivera**  
Secretary of State

**Luis Sánchez Betances**  
Secretary of Justice

**Melba I. Acosta Febo**  
Secretary of the Treasury

**Rafael Román Meléndez**  
Secretary of Education

**Vance Thomas Rider**  
Secretary of Labor and  
Human Resources

**Ana C. Rius Armendariz**  
Acting Secretary of Health

**Myrna Comas Pagán**  
Secretary of Agriculture

**Miguel Torres Díaz**  
Secretary of Transportation and  
Public Works

**Alberto Bacó Bagué**  
Secretary of Economic  
Development and Commerce

**Idalia Colón Rondón**  
Secretary of Family Affairs

**Rubén Ríos Pagán**  
Secretary of Housing

**Carmen R. Guerrero Pérez**  
Secretary of Natural and  
Environmental Resources

**Nery E. Adames Soto**  
Secretary of Consumer Affairs

**Ramón E. Orta Rodríguez**  
Secretary of Sports and  
Recreation

**José R. Negrón Fernández**  
Secretary of Corrections and  
Rehabilitation

---

### LEGISLATIVE OFFICERS

**Eduardo Bhatia Gautier**  
President, Senate

**Jaime Perelló Borrás**  
Speaker, House of  
Representatives

---

### FISCAL OFFICERS

**Carlos Rivas Quiñones**  
Director, Office of Management  
and Budget

**José Pagán Beauchamp**  
Acting President, Government  
Development Bank for  
Puerto Rico



Deloitte & Touche LLP  
Torre Chardon  
350 Chardon Ave.  
Suite 700  
San Juan, PR 00918-2140  
USA  
Tel: +1 787 759 7171  
Fax: +1 787 756 6340  
[www.deloitte.com](http://www.deloitte.com)

## INDEPENDENT AUDITORS' REPORT

To the Honorable Governor and Legislature  
Commonwealth of Puerto Rico  
San Juan, Puerto Rico

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth of Puerto Rico (the "Commonwealth"), as of and for the year ended June 30, 2012, which collectively comprise the Commonwealth's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Commonwealth's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the following activities, funds, and component units:

- Puerto Rico Public Housing Administration, Labor Development Administration, the Office for the Administration of the Assets of the Urban Renovation and Housing Corporation of the Commonwealth of Puerto Rico, and the Office for the Improvements of Public Schools, which collectively represent 18% and 3%, respectively, of the assets and revenues of the governmental activities and 29% and 4%, respectively, of the assets and revenues of the general fund;
- The Unemployment Insurance Fund, which is both a major fund and 36% and 38%, respectively, of the assets and revenues of the business-type activities. The Additional Lottery System, which represents 68% and 50%, respectively, of the assets and revenues of the lotteries fund and 10% and 28%, respectively, of the assets and revenues of the business-type activities. The Disability Insurance Fund, the Drivers' Insurance Fund, the Puerto Rico Water Pollution Control Revolving Fund and the Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund, which represent 54% and 5%, respectively, of the assets and revenues of the business-type activities and 7% and 4%, respectively, of the assets and revenues of the aggregate remaining fund information;
- Public Buildings Authority special revenue, debt service, and capital project funds; The Children's Trust special revenue and debt service funds; and the Puerto Rico Maritime Shipping Authority debt service fund, which collectively represent 9% and .28%, respectively, of the assets and revenues of the governmental activities and 13% and 3%, respectively, of the assets and revenues of the aggregate remaining fund information;
- Entities identified in note 2 that are presented as discretely presented component units, which collectively represent 72% and 92%, respectively, of the assets and revenues of the aggregate discretely presented component units.

Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for the activities, funds, and component units indicated above, are based solely on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Commonwealth's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth, as of June 30, 2012, and the respective changes in financial position and, where applicable, cash flows thereof and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 20 to the basic financial statements, the Pension Trust Funds' unfunded actuarial accrued liability and funded ratio as of June 30, 2012, were approximately \$37,017 million and 8.4%, respectively. In the opinion of management, based on information prepared by consulting actuaries, the net assets of the Employee's Retirement System of the Government of the Commonwealth of Puerto Rico, the Commonwealth of Puerto Rico Judiciary Retirement System, and the Puerto Rico System of Annuities and Pensions for Teachers, comprising the Pension Trust Funds, will be exhausted by the fiscal years 2015, 2019, and 2021, respectively, if measures are not implemented to reduce the unfunded actuarial accrued liability and increase the funded ratio of the Pension Trust Funds. Management's plans concerning this matter are also described in Note 20.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 20 through 33 and the schedules of funding progress on pages 240 and 241 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Commonwealth's financial statements. The combining and individual nonmajor fund financial statements and schedules are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial

statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, based on our audit and the reports of other auditors, the combining and individual nonmajor fund financial statements and schedules are fairly stated in all material respects in relation to the financial statements as a whole.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Commonwealth's basic financial statements. The introductory and statistical sections are presented for the purposes of additional analysis and are not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

*Deloitte & Touche LLP*

September 16, 2013

Stamp No. E85052  
affixed to original.

## COMMONWEALTH OF PUERTO RICO

### MANAGEMENT'S DISCUSSION AND ANALYSIS<sup>1</sup> JUNE 30, 2012

---

The following is a narrative overview and analysis of the financial activities of the Commonwealth of Puerto Rico (the "Commonwealth" or the "Government") for the fiscal year ended June 30, 2012. The management discussion and analysis ("MD&A") is intended to serve as an introduction to the basic financial statements, which have the following components: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the financial statements. The MD&A is designed to: (a) assist the reader in focusing on significant financial matters; (b) provide an overview of the Commonwealth's financial activities; (c) identify any material changes from the original budget; and (d) highlight individual fund matters. We encourage readers to review this information in conjunction with the Letter of Transmittal, which is located in the Introductory Section of this report, and the Commonwealth's basic financial statements, including the notes to the financial statements, which are located after this analysis.

### MAJOR FINANCIAL ELEMENTS

*Revenues* — The General Fund is the primary operating fund of the Commonwealth. General Fund revenues are broadly based and include revenues raised internally as well as those from non-Puerto Rico sources. Internal revenues consist principally of income tax, sales and use tax, and excise tax. Revenues from non-Puerto Rico sources are derived from federal excise taxes and customs duties returned to the Commonwealth. The major source of revenue from the component units are charges for services.

*Expenditures* — Expenditures consist principally of grants and subsidies, personal services, other services, materials and supplies, equipment purchases, capital outlays, debt service and transfers.

*Debt* — Comprises bonds and notes of the Commonwealth and component units. The Commonwealth's policy has been and continues to be to prudently manage its debt within the constitutional limitation. Debt of component units, other than bond anticipation notes, is generally supported by the revenues of such units from rates charged for services or products and Commonwealth's pledged revenues. However, certain debt of component units is supported, in whole or in part, directly or indirectly, by Commonwealth appropriations or taxes. Direct debt of the Commonwealth is issued pursuant to specific legislation approved in each particular case. Debt of component units is issued in accordance with their enabling statutes. Government Development Bank for Puerto Rico ("GDB"), as fiscal agent of the Commonwealth, must approve the specific terms of each debt issuance.

---

<sup>1</sup> The management's discussion and analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Commonwealth's management. The independent auditors have applied certain limited procedures, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge they obtained during the audit of the basic financial statements. Therefore, the independent auditors did not audit such information and did not express an opinion nor provide any assurance on it.

The infrastructure assets representing items that are normally immovable and of value only to the Commonwealth as roads, highways, bridges, toll facilities, water and sewer systems, lighting production, transmission and distribution systems, and similar items are principally owned by the component units of the Commonwealth. Therefore, the infrastructure assets are reported within depreciable capital assets under the discretely presented component units' column. Additional information on the Commonwealth's capital assets can be found in Note 13 to the basic financial statements that accompany this report.

**COMMONWEALTH'S CAPITAL ASSETS — PRIMARY GOVERNMENT**  
**JUNE 30, 2012**  
**(Expressed in thousands)**

	<b>Governmental Activities</b>	<b>Business-Type Activities</b>
Land	\$ 878,881	\$ -
Construction in progress	1,487,071	-
Buildings and building improvements, net	5,124,347	-
Equipment, furniture, fixtures, vehicles and software, net	193,535	1,726
Infrastructure, net	<u>461,966</u>	<u>-</u>
 Total capital assets	 <u>\$8,145,800</u>	 <u>\$ 1,726</u>

***Debt Administration***

Total long-term obligations of the primary government as of June 30, 2012 were \$51.7 billion, of which \$2.0 billion are due within one year. Long-term obligations of the primary government increased by \$5.9 billion, or 13%, when compared to the prior fiscal year.

General obligation bonds are backed by the full faith and credit of the Commonwealth, including the Commonwealth's power to levy additional taxes to help ensure repayment of the debt.

The Constitution of the Commonwealth provides that direct obligations of the Commonwealth evidenced by bonds or notes and backed by the full faith, credit, and taxing power of the Commonwealth are not to be issued if the amount of the principal of, and interest on, such bonds and notes and on all such bonds and notes issued thereafter, which are payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on account of bonds or notes guaranteed by the Commonwealth, exceed 15% of the average annual revenue raised under the provisions of Commonwealth legislation and conveyed into the treasury (internal revenues) in the two fiscal years preceding the current fiscal year. Section 2, Article VI of the Constitution of the Commonwealth does not limit the amount of debt that the Commonwealth may guarantee as long as the 15% limitation is not exceeded through payments by the Commonwealth on such guaranteed debt. At June 30, 2012, the Commonwealth is in compliance with the debt limitation requirement.

The Commonwealth's policy has been and continues to be to prudently manage such debt within the constitutional limitation. Debt of municipalities, other than bond anticipation notes, is supported by real and personal property taxes, municipal license taxes, and the corresponding part of the sales and use tax. Debt of public corporations, other than bond anticipation notes, is generally supported by the revenues of such corporations from rates charged for services or products. However, certain debt of public corporations is supported, in whole or in part, directly or indirectly, by Commonwealth appropriations or taxes.

Internal revenues consist principally of income taxes, property taxes, sales and use taxes and excise taxes. Certain revenues, such as federal excise taxes on offshore shipments of alcoholic beverages and tobacco

products and customs duties, which are collected by the United States Government and returned to the Treasury Department of Puerto Rico and motor vehicle fuel taxes and license fees, which are allocated to the Highways and Transportation Authority, are not included as internal revenues for the purpose of calculating the debt limit, although they may be available for the payment of debt service. In addition, the portion of the sales and use tax allocated to COFINA is not included as internal revenues since the legislation that created COFINA transferred ownership of such portion of the sales and use tax to COFINA and provided that such portion was not available resources under the Constitutional provisions relating to full faith and credit bonds.

The Commonwealth's general obligation and appropriation debt is currently rated "Baa3" with a negative outlook by Moody's, "BBB-" with a negative outlook by Fitch, and "BBB-" with a negative outlook by S&P.

Additional information on the Commonwealth's long term debt can be found in Note 15 to the basic financial statements that accompany this report.

### **General Fund Budgetary Highlights**

The Commonwealth adopts an annual appropriated budget for its General Fund. A budgetary comparison statement has been provided for the General Fund to demonstrate compliance with this budget. The statement of revenue and expenditures — budget and actual — budget basis — general fund only presents the information for the general fund for which there is a legally adopted budget, as required by US GAAP. See Note 3 to the basic financial statement for a reconciliation of the statement of revenue and expenditures — budget and actual — budget basis — general fund with the statement of revenues, expenditures, and changes in fund balance (deficit) for the general fund. This statement is presented on the page immediately following the reconciliation of the statement of revenues, expenditures, and changes in fund balances (deficit) to the statement of activities — governmental funds.

Total General Fund actual revenues on a budget basis (sources) for fiscal year 2012 was \$8.6 billion, (excluding other financing source) representing an increase of approximately \$51.5 million, or 6%, from original budgeted revenues and an increase of approximately \$579 million from actual revenues of \$7.9 billion for fiscal year 2011.

Total actual expenditures on a budget basis of \$9.9 billion represented an increase of \$836 million when compared with fiscal year 2011.

For fiscal year 2012, the actual budgetary deficit in the General Fund was \$1.3 billion, consisting of the difference between total recurring revenues of \$8.6 billion and total expenditures for such fiscal year of \$9.9 billion. For fiscal year 2011, the deficit was \$1.1 billion, consisting of the difference between total recurring revenues of \$8 billion and total expenditures for such fiscal year of \$9.1 billion. The deficits for fiscal years 2012 increased by 23% when compared to 2011 and decreased by 47% when compared to the deficit in 2010. The Government's ability to continue reducing the deficit will depend in part on its ability to continue increasing revenues and reducing expenditures, which in turn depends on a number of factors, including improvements in general economic conditions.

***Differences Between Budget and Basic Financial Statements*** — Revenues and expenditures, as reported by the Treasury Department in its basic financial statements, may differ substantially from resources and appropriations in its annual budget for a number of reasons, including the following:

- The budgetary accounts are on a budgetary basis, while financial statements prepared by the Treasury Department include adjustments as required by government accounting standards.

## COMMONWEALTH OF PUERTO RICO

### NOTES TO BASIC FINANCIAL STATEMENTS AS OF AND FOR THE YEAR ENDED JUNE 30, 2012

---

#### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Commonwealth of Puerto Rico (the “Commonwealth”) was constituted on July 25, 1952, under the provisions of the Commonwealth’s Constitution (the “Constitution”) as approved by the people of Puerto Rico and the U.S. Congress. The Constitution provides for the separation of powers of the executive, legislative, and judicial branches of the government. The Commonwealth assumes responsibility for general government, public safety, health, public housing and welfare, education, and economic development.

The accompanying basic financial statements of the Commonwealth are presented in conformity with Accounting Principles Generally Accepted in the United States of America (US GAAP) for governments as prescribed by the Governmental Accounting Standards Board (GASB).

The accompanying basic financial statements present the financial position of the Commonwealth and its various funds, the results of operations of the Commonwealth and its various funds and fund types, and the cash flows of the proprietary funds. The basic financial statements are presented as of June 30, 2012 and for the year then ended. The basic financial statements include the various departments, agencies, boards, commissions, public trusts and public corporations, and any other organizational units governed by the Puerto Rico Legislature and/or officers of the Commonwealth.

##### **(a) Financial Reporting Entity**

The basic financial statements of the Commonwealth include all departments, agencies, and governmental entities whose funds are under the custody and control of the Secretary of the Treasury of the Commonwealth and the Commonwealth’s component units pursuant to Act No. 230 of July 23, 1974, as amended, known as Commonwealth of Puerto Rico Accounting Law. The Commonwealth has considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the Commonwealth are such that exclusion would cause the Commonwealth’s basic financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include: (i) appointing a voting majority of an organization’s governing body and the ability of the Commonwealth to impose its will on that organization or (ii) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the Commonwealth.

As required by US GAAP, these basic financial statements present the Commonwealth and its component units.

##### **(b) Component Units**

Component units are entities that are legally separate organizations for which the Commonwealth’s elected officials are financially accountable or other organizations for which the nature and significance of their relationship with the Commonwealth are such that exclusion would cause the Commonwealth’s basic financial statements to be misleading or incomplete. US GAAP details two methods of presentation: (i) blending the financial data of the component units’ balances and

## 15. SHORT AND LONG-TERM OBLIGATIONS

### (a) Primary Government

*Summary of Short and Long-term Obligations* — Short and long-term obligations at June 30, 2012 and changes for the year then ended are as follows (expressed in thousands):

Short-Term Obligations	Balance At June 30, 2011 (As restated)	Debt Issued	Debt Paid	Debt Refunded	Original Issue Premium, net	Other Net Increases (Decreases)	Balance At June 30, 2012	Due Within One Year
Notes payable to GDB	\$ 32,179	\$ 153,831	\$ (155,329)	\$ -	\$ -	\$ (13,797)	\$ 16,884	\$ 16,884
Bond anticipation notes payable	<u>-</u>	<u>79,144</u>	<u>(3,309)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>75,835</u>	<u>75,835</u>
<b>Short-Term Obligations</b>								
Notes payable to GDB	<u>\$ 32,179</u>	<u>\$ 232,975</u>	<u>\$ (158,638)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (13,797)</u>	<u>\$ 92,719</u>	<u>\$ 92,719</u>
<b>Long-Term Obligations</b>								
Governmental activities:								
General obligation and revenue bonds	\$ 29,126,136	\$ 6,640,840	\$ (382,282)	\$ (2,303,973)	\$ 12,684	\$ 98,589	\$ 33,191,994	\$ 468,485
Commonwealth appropriation bonds	<u>743,184</u>	<u>564,323</u>	<u>(310,179)</u>	<u>(483,666)</u>	<u>5,729</u>	<u>13,520</u>	<u>532,911</u>	<u>-</u>
Notes payable to component units:								
GDB	1,648,777	966,537	(1,044,186)	-	-	13,797	1,584,925	96,462
Other	68,918	-	(37,925)	-	-	-	30,993	19,273
Capital leases	<u>229,574</u>	<u>680</u>	<u>(5,819)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>224,435</u>	<u>9,500</u>
Total bonds, notes, and capital leases payable	31,816,589	8,172,380	(1,780,391)	(2,787,639)	18,413	125,906	35,565,258	593,720
Compensated absences	1,431,424	-	-	-	-	(55,454)	1,375,970	679,649
Net pension obligation	9,325,352	-	-	-	-	1,833,449	11,158,801	-
Net postemployment benefit obligation	174,918	-	-	-	-	40,326	215,244	-
Voluntary termination benefits payable	332,905	-	-	-	-	320,620	653,525	63,918
Other long-term liabilities	<u>2,325,463</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>96,116</u>	<u>2,421,579</u>	<u>572,915</u>
Total governmental activities	<u>45,406,651</u>	<u>8,172,380</u>	<u>(1,780,391)</u>	<u>(2,787,639)</u>	<u>18,413</u>	<u>2,360,963</u>	<u>51,390,377</u>	<u>1,910,202</u>
Business-type activities:								
Compensated absences	4,812	-	-	-	-	156	4,968	2,711
Obligation for unpaid lottery prizes	218,486	-	-	-	-	(26,900)	191,586	49,883
Voluntary termination benefits payable	2,641	-	-	-	-	2,601	5,242	587
Claims liability for insurance benefits	<u>86,338</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(13,344)</u>	<u>72,994</u>	<u>72,994</u>
Total business-type activities	<u>312,277</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(37,487)</u>	<u>274,790</u>	<u>126,175</u>
Total primary government	<u>\$ 45,718,928</u>	<u>\$ 8,172,380</u>	<u>\$ (1,780,391)</u>	<u>\$ (2,787,639)</u>	<u>\$ 18,413</u>	<u>\$ 2,323,476</u>	<u>\$ 51,665,167</u>	<u>\$ 2,036,377</u>

The principal balance of general obligation and revenue bonds paid reported as expenditures in the statement of revenues, expenditures, and changes in fund balances (deficit) — governmental funds does not agree with amounts reported as debt paid in the table above because it includes principal paid on July 1, 2011 on general obligation and revenue bonds amounting to approximately \$334 million, which was accrued at June 30, 2011 as a fund liability. Also, during fiscal year 2012 the amount of approximately \$425 million of debt principal paid on July 1, 2012 was accrued as a fund liability at June 30, 2012, but not included as payments in the table above. The net effect of \$91 million is the difference between the principal paid on bonds, notes and capital leases payable included in the previous table and the principal shown as expenditures in the statement of revenues, expenditures, and changes in fund balances (deficit) — governmental funds.

On November 23, 2011, COFINA issued its Series 2011A-2 capital appreciation bonds amounting to approximately \$337 million in satisfaction of the redemption price on certain outstanding subordinated capital appreciation bonds. Since there was no cash involved in this transaction, the issuance and the repayment of such bonds were excluded from the table above.

Other net increases (decreases) include an increase of \$13.8 million in notes payable to GDB, which were classified as short term at June 30, 2011, but which terms were formally extended to a longer term during fiscal year 2012 and, consequently, reclassified as long term and presented as a new long term debt issued in the statement of revenues, expenditures, and changes in fund balances (deficit) — governmental funds. The remaining balance of the other net increases (decreases) in bonds, notes and capital leases payable consists of capitalization of interest on capital appreciation bonds; deferred gains/losses on refunding's, net of amortization; amortization of premiums and accretion of discounts on bonds and notes payable. These adjustments did not require any source or use of cash.

Compensated absences, net pension obligation, net postemployment benefit obligation, termination benefits, other long-term liabilities, obligation for unpaid lottery prizes, and claims liability for insurance benefits reflect other net increases (decreases) resulting from adjustments and changes to agree these obligations to their new estimated balances at June 30, 2012.

#### **(b) Debt Limitation**

The Constitution of the Commonwealth authorizes the contracting of debts as determined by the Legislature. Nevertheless, Section 2, Article VI of the Constitution of the Commonwealth provides that direct obligations of the Commonwealth evidenced by bonds or notes and backed by the full faith, credit, and taxing power of the Commonwealth shall not be issued if the amounts of the principal of and interest on such bonds and notes and on all such bonds and notes issued thereafter, which are payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year of such proposed issuance on account of bonds or notes guaranteed by the Commonwealth, exceed 15% of the average annual revenues raised under the provisions of Commonwealth legislation and deposited into the Treasury (hereinafter "internal revenues") in the two fiscal years preceding the fiscal year of such proposed issuance. Section 2, Article VI of the Constitution does not limit the amount of debt that the Commonwealth may guarantee so long as the 15% limitation is not exceeded through payments by the Commonwealth on such guaranteed debt. Internal revenues consist principally of income taxes, sales and use tax, property taxes and excise taxes. Certain revenues, such as federal excise taxes on offshore shipments of alcoholic beverages and tobacco products and customs duties, which are collected by the United States Government and returned to the Commonwealth, and motor vehicle fuel taxes, crude oil and derivative products excise taxes and license fees, which are allocated to PRHTA, a discrete component unit, are not included as revenues for the purpose of calculating the debt limit, although they may be available for the payment of debt service. In addition, the portion of sales and use tax allocated to COFINA is not

included as internal revenues consistent with the legislation creating COFINA, which transfers ownership of such portion of the sales and use tax to COFINA and provides that such portion is not "available resources" under the constitutional provisions relating to the payment of debt service. At June 30, 2012, the Commonwealth is in compliance with the debt limitation requirement.

**(c) Bonds Payable**

The Constitution of the Commonwealth provides that public debt will constitute a first claim on the available revenue of the Commonwealth. Public debt includes general obligations and revenue bonds of the Commonwealth and any payment required to be made by the Commonwealth under its guarantees of bonds issued by blended or discretely presented component units. The full faith, credit, and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal and interest of the general obligation bonds.

Act No. 83 of August 30, 1991, as amended, provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation. The levy is made by Municipal Revenue Collection Center (CRIM by its Spanish acronym), a municipal corporation, not a component unit of the Commonwealth. CRIM is required to remit the 1.03% of property tax collected to the Commonwealth to be used by the Commonwealth's debt service fund for payment of debt service on general obligations and revenue bonds of the Commonwealth. During the year ended June 30, 2012, the total revenue and receivable reported by the Commonwealth amounted to approximately \$115 million and \$32 million, respectively, which are included in the debt service fund.

For financial reporting purposes, the outstanding amount of bonds represents the total principal to be repaid, plus unamortized premiums and interest accreted on capital appreciation bonds, less unaccreted discount and deferred refunding losses.

## **STATISTICAL SECTION (UNAUDITED)**

This part of the Commonwealth of Puerto Rico's comprehensive annual financial report presents detailed information as a context for understanding what the information in the financial statements, note disclosures, and required supplementary information says about the Commonwealth's overall financial health. The following are the categories of the various schedules that are included in this Section:

Contents	Pages
<b>Financial Trends Information</b>	283–287
These schedules contain trend information to help the reader understand how the Commonwealth's financial performance and well-being have changed over time.	
<b>Revenue Capacity Information</b>	289–290
This schedule contains information to help the reader assess the Commonwealth's most significant local revenue sources.	
<b>Debt Capacity Information</b>	292–293
These schedules present information to help the reader assess the affordability of the Commonwealth's current levels of outstanding debt and the Commonwealth's ability to issue additional debt in the future.	
<b>Demographic and Economic Information</b>	295–297
These schedules offer demographic and economic indicators to help the reader understand the environment within which the Commonwealth's financial activities take place.	
<b>Operating Information</b>	299
This schedule contains service data to help the reader understand how the information in the Commonwealth's financial report relates to the services the government provides and the activities it performs.	
Sources: Unless otherwise noted, the information in these schedules is derived from the comprehensive annual financial reports for the relevant year.	

## **SCHEDULES OF DEBT CAPACITY INFORMATION**

## COMMONWEALTH OF PUERTO RICO

### LEGAL DEBT MARGIN INFORMATION (UNAUDITED) LAST TEN FISCAL YEARS (In thousands)

	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
Internal revenue average for two years	\$ 8,092,987	\$7,592,395	\$ 7,333,246	\$ 7,650,006	\$ 8,233,717	\$ 8,327,744	\$ 8,061,593	\$ 7,779,987	\$ 7,564,034	\$ 7,185,660
Legal debt limit — 15% of internal revenue average for two years	1,213,948	1,138,859	1,099,987	1,147,501	1,235,058	1,249,162	1,209,239	1,166,998	1,134,605	1,077,849
Maximum debt service requirement	964,416	876,205	826,812	785,298	785,298	719,927	680,742	630,685	598,547	599,611
Additional legal debt service requirement margin	249,532	262,654	273,175	362,203	449,760	529,235	528,497	536,313	536,058	478,238
Total maximum debt service requirement as a percentage of internal revenue average for two years	11.92 %	11.54 %	11.27 %	10.27 %	9.54 %	8.64 %	8.44 %	8.11 %	7.91 %	8.34 %
Legal debt margin calculation for fiscal year 2012:										
Internal revenue for the year ended June 30, 2011							\$ 7,828,135			
Internal revenue for the year ended June 30, 2012							<u>8,357,838</u>			
Total internal revenue for the years ended June 30, 2011 and 2012							<u>16,185,973</u>			
Internal revenue average for the two years							8,092,987			
Legal debt limit — 15% of internal revenue average for the two years							<u>1,213,948</u>			
Maximum debt service requirement							<u>964,416</u>			
Additional legal debt service requirement as a percentage of internal revenue average for two years							<u>\$ 249,532</u>			

Sources: Government Development Bank for Puerto Rico, General obligation debt service may not exceed 15% of the average of the internal revenues for the last two fiscal years.